[COMMITTEE PRINT]

DESCRIPTION OF PROPOSALS RELATING TO ESTATE AND GIFT TAX CHANGES AND OTHER PROPOSED AMENDMENTS TO H.R. 6715 AND H.R. 9251

PREPARED FOR THE USE OF THE

COMMITTEE ON FINANCE

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

NOVEMBER 9, 1977

U.S. GOVERNMENT PRINTING OFFICE

98-286 WASHINGTON : 1977 JCS-64-77

CONTENTS

INTRODUCTION

This pamphlet describes various proposed amendments to be considered in connection with H.R. 6715 (the Technical Corrections Act), H.R. 9251 (the Tax Treatment Extension Act), and other revenue bills before the Committee.

The first part of the pamphlet compares alternative proposals relating to carryover basis and other proposals to the estate and gift taxes included in H.R. 6715 (Technical Corrections Act), S. 1954 (Senator Curtis), S. 2227 (Senators Byrd, of Virginia and Dole), S. 2228 (Senators Byrd, of Virginia and Dole), and S. 2238 (Senator Hathaway). This comparison also gives the Treasury Department's position on the proposed changes.

The second part describes amendments to H.R. 6715 proposed by the Treasury Department.

The third part of the pamphlet describes other proposed amendments submitted by members of the Committee.

I. COMPARISON OF BILLS RELATING TO CARRYOVER BASIS AND ESTATE AND GIFT TAX CHANGES

A. Proposals to Repeal or Suspend Carryover Basis

Tax Reform Act of 1976

Under the Tax Reform Act of 1976, the basis of property passing from a decedent is "carried over" from the decedent to the estate or heir. Basis adjustments are made for (1) certain death taxes attributable to appreciation, (2) appreciation arising prior to 1977 (the so-called "fresh start" adjustment), and (3) a $60,000 minimum basis. The provision applies with respect to property passing from decedents dying after December 31, 1976.

Proposals

Repeal of carryover basis.—S. 1954 (introduced by Senator Curtis) would repeal the carryover basis provision in the 1976 Act.

Suspension of carryover basis.—S. 2227 (introduced by Senators Byrd of Virginia and Dole) provides for a 2-year suspension of the effective date of the carryover basis provision so that it would apply only with respect to property acquired from a decedent dying after December 31, 1978.

I. COMPARISON OF BILLS RELATING TO CARRYOVER BASIS AND ESTATE AND GIFT TAX CHANGES—(Con.)

B. Proposals Relating to Carryover Basis

Item	Present law	H.R. 6715
1. General rule	Under the Tax Reform Act of 1976, the basis of property passing from a decedent is "carried over" from the decedent to the estate or heir. Basis adjustments are made for (1) certain death taxes attributable to appreciation, (2) appreciation arising prior to 1977 (the so-called "fresh start" adjustment), and (3) a $60,000 minimum basis. The provision applies with respect to property passing from decedents dying after December 31, 1976.	Retains general rule but makes correcting and technical changes.
2. Fresh start adjustment		
Increase in basis	Provides for an increase in basis for appreciation arising before 1977 for carryover basis property held on that date.	

I. COMPARISON OF BILLS RELATING TO CARRYOVER BASIS AND ESTATE AND GIFT TAX CHANGES—(Con.)

B. Proposals Relating to Carryover Basis

S. 2228 (Byrd/Dole)	S. 2238 (Hathaway)	Treasury Position
Retains general rule but makes simplifying, correcting, and technical changes.	Retains general rule but makes simplifying, correcting, and technical changes.	Generally supports S. 2238. Strongly opposes S. 1954 and S. 2227.
Grandfathers property held on 12/31/76. Repeals the "fresh start" basis adjustment.		Strongly opposes grandfather provision of S. 2228.

98–286—77——2

B. Proposals Relating to Carryover Basis—Continued

Item	Present law	H.R. 6715
2. ***Fresh start adjustment*—Con.**		
Marketable property	For marketable property, the adjustment is based on fair market value on 12/31/76.	
Nonmarketable property	For nonmarketable property, the value of an asset on 12/31/76 is determined by apportioning the appreciation on the basis of holding period before 1977 compared to the total holding period.	Provides formula to determine minimum basis for fresh start purposes. It assumes that post-1976 appreciation accrues at approximately 8%/year. The rule applies only to tangible personal property.
Gain or loss adjustment	The "fresh start" adjustment is made for gain purposes but not for loss purposes.	
3. ***Minimum basis adjustment***		
Amount	Provides for a $60,000 minimum basis adjustment.	
Order of adjustments	Minimum basis adjustment is made after fresh start and death tax adjustments.	

B. Proposals Relating to Carryover Basis—Continued

S. 2228 (Byrd/Dole)	S. 2238 (Hathaway)	Treasury Position
	Extends marketable property rule to certain preferred stock.	Does not oppose.
	Provides same formula as H.R. 6715 except it applies to nonbusiness personal property and personal residence.	Supports S. 2238 if intangible assets are excluded.
	Fresh start adjustment to be made for loss purposes as well as gain.	Does not oppose.
Increases minimum basis to $175,000 in 1981. Phased-in from $120,000 beginning in 1977.	Same as S. 2228.	Supports, but would increase minimum basis to $175,000 immediately.
Minimum basis adjustment made before death tax adjustment.	Same as S. 2228.	Supports.

B. Proposals Relating to Carryover Basis—Continued

Item	Present law	H.R. 6715
4. Death tax adjustments		
Number and method of computing adjustments	Adjustments to basis are provided for death taxes attributable to appreciation. Separate adjustments made for Federal estate taxes, State death taxes paid by estate, and State death taxes paid by beneficiary.	Clarifies that State death tax adjustment is made on basis of State inclusion rules.
Type of property adjusted	Adjustments are made only for property subject to tax, i.e. no adjustment made for marital and charitable deduction property.	
Amount of adjustment	Amount of adjustment determined on basis of average death tax rates.	

B. Proposals Relating to Carryover Basis—Continued

S. 2228 (Byrd/Dole)	S. 2238 (Hathaway)	Treasury Position
Combines death tax adjustments into single adjustment to be made on basis of Federal inclusion rules.	Same as S. 2228.	Supports concept of simplified single adjustment described below.
Adjustments made to all property including charitable and marital deduction property.	Same as S. 2228.	No adjustment for property funding marital, charitable or orphan's bequests.
Amount of adjustment determined on basis of marginal death tax rates.	Same as S. 2228.	Prefer adjustment to be computed as follows: (1) Single adjustment at highest marginal Federal estate rate if in bracket by $50,000. (2) No adjustment if Federal estate tax return not required. (3) Allow adjustment for nontaxable estates for which returns are required at schedule rates.

B. Proposals Relating to Carryover Basis—Continued

Item	Present law	H.R. 6715
5. *Information returns*	Executor is required to file with IRS and furnish carryover basis information to heir receiving property (sec. 6039A). Penalties are imposed for failure to do so (sec. 6694).	
6. *Inherited art work, literary work and similar property*	Capital gain treatment is not available for art work, literary work and similar property inherited from its creator.	
7. *Inherited carryover basis—crops and livestock*	No special rule is provided to extend capital gain treatment to inherited crops or livestock.	
8. *Net operating and capital loss carryovers*	Net operating and capital loss carryovers which were unused by the decedent do not carry over to the estate.	

B. Proposals Relating to Carryover Basis—Continued

S. 2228 (Byrd/Dole)	S. 2238 (Hathaway)	Treasury Position
Carryover basis information is not required to be filed or furnished if the gross estate is less than $175,000 (phased-in from $120,000 in 1977 to $175,000 in 1981).	Same as S. 2228.	Supports, but would not phase-in increase.
Extends capital gain treatment to inherited art work, literary work and similar property.		Does not oppose.
Extends capital gain treatment to inherited crops and livestock, whether or not considered inventory in hands of estate or beneficiary.		Prefers that inherited crops and livestock in hands of the estate be eligible for maximum tax.
Provides that decedent's unused loss carryovers are carried over to the estate.		Opposes net operating loss carryovers. Does not oppose capital loss carryover.

I. COMPARISON OF BILLS RELATING TO CARRYOVER BASIS AND ESTATE AND GIFT TAX CHANGES—(Con.)

C. Proposals Relating to Estate and Gift Tax Provisions

Item	Present law	H.R. 6715
1. Transfers within 3 years of death	Transfers made within 3 years of death are included in the decedent's gross estate.	Makes it clear that gifts eligible for $3,000 annual gift tax exclusion are not included in gross estate (exception for life insurance).
2. Special use valuation		
General rule	Qualifying farm and closely held business real property may be valued at current use value rather than highest and best use.	Several clarifying changes made.
Material participation	Decedent or member of family must have materially participated in operation for 5 out of 8 years preceding decedent's death.	
	Estate tax savings are recaptured if there are periods of aggregating 3 years or more during which there is no material participation by qualified heir or member of his family.	

I. COMPARISON OF BILLS RELATING TO CARRYOVER BASIS AND ESTATE AND GIFT TAX CHANGES—(Con.)

C. Proposals Relating to Estate and Gift Tax Provisions

S. 2228 (Byrd/Dole)	S. 2238 (Hathaway)	Treasury Position
Repeals transfer within 3-year-of-death rule except for life insurance and transfers where decedent had retained "strings."	Continues present law (as amended by H.R. 6715), but with gift tax valuations used. Not applicable to life insurance or transfers where decedent retained "strings."	Supports S. 2238.
Material participation requirement is met if decedent or surviving spouse had materially participated for 20 years.	Same as S. 2228.	Does not oppose.
Operation by an agent counts as material participation for qualified heir who is (1) minor; (2) student; (3) handicapped; or (4) surviving spouse age 62 or over.	Same as S. 2228.	Does not oppose.

C. Proposals Relating to Estate and Gift Tax Provisions—Con.

Item	Present law	H.R. 6715
3. Stock redemptions to pay death taxes		
General rule—capital gains	Capital gains treatments is available for redemptions of closely held stock to pay death taxes and administration expenses (sec. 303).	Provides that capital gains treatment is available for certain closely held preferred stock (sec. 306 stock).
Percentage requirement	Value of stock must be 50% of gross estate reduced by debts and administration expenses.	
4. Definition of interest in closely held business for estate tax extended payment provisions	Two extended payment provisions are provided for estate taxes attributable to a closely held business. One provides a 10-yr. payment period (sec. 6166A) and the other a 15-year period (sec. 6166).	
Number of shareholders or partners	For the 15-year extension, a closely held business interest includes an interest in a corporation or partnership having 15 or fewer shareholders or partners. For the 10-year extension, the interest includes an interest in a corporation or partnership having 10 or fewer shareholders or partners.	

C. Proposals Relating to Estate and Gift Tax Provisions—Con.

S. 2228 (Byrd/Dole)	S. 2238 (Hathaway)	Treasury Position
Extends capital gains treatment to cover redemptions to pay income taxes attributable to redemptions to pay death taxes.		Opposes S. 2228. Supports H.R. 6715.
Special treatment also available if value of stock is 35% of gross estate.		Opposes.
Conforms the two definitions so that the rule for 15 shareholders or partners applies for both extended payment rules.	Same as S. 2228.	Does not oppose.

D. Estimated Revenue Effect of Bills Relating to Carryover Basis Proposals and Other Estate and Gift Tax Changes

Table 1.—Revenue Effect of S. 1954 (Senator Curtis): Repeal of the Carryover Basis Provisions of the Tax Reform Act of 1976

(millions of dollars)

Provision	Fiscal year— 1978	1979	1980	1981	1982	Long run [1]
Repeal of carryover basis	([2])	−36	−93	−162	−238	−1,080

[1] 18 to 20 years.
[2] Less than $1 million.

Table 2.—Revenue Effect of S. 2227 (Senators Byrd of Virginia and Dole): Postponement of the Carryover Basis Provisions of the Tax Reform Act of 1976

(millions of dollars)

Provision	Fiscal year— 1978	1979	1980	1981	1982	Long run [1]
2-yr postponement of carryover basis	([2])	−36	−93	−76	−63	0

[1] 18 to 20 years.
[2] Less than $1 million.

Table 3.—Revenue Effect of S. 2228 (Senators Byrd of Virginia and Dole): Amending the Carryover Basis Provisions of the Tax Reform Act of 1976

(millions of dollars)

Provision	Fiscal year— 1978	1979	1980	1981	1982	Long run [1]
"Grandfathering" Dec. 31, 1976 property	([3])	−36	−86	−146	−209	0
Increased minimum basis				−23	−39	−243
Single basis adjustment	([2])	([2])	([2])	([2])	([2])	([2])
Marginal rate basis adjustment				−9	−18	−109
Allocation of basis adjustment				+3	+6	+35
Art and literary work treated as capital asset	([2])	([2])	([2])	([2])	([2])	([2])
Crops and livestock as capital asset	([3])	−10	−14	−19	−24	−24
Gross estate includes gift tax and life insurance transferred within 3 yrs. of death	([4])	([4])	([4])	([4])	([4])	([4])
Material participation rule for farm valuation	([3])	([3])	([3])	([3])	([3])	([3])
Estate succeeds to decedent's NOL's and capital loss carryovers	([4])	([4])	([4])	([4])	([4])	([4])
Capital gains treatment for redemptions of closely held stock to pay income taxes on redemptions to pay death taxes	−1	−2	−3	−4	−5	−17
Capital gains treatment for stock redemptions if value of stock is more than 35 percent of gross estate	([3])	([3])	([3])	([3])	([3])	([3])
Closely held business definition	([3])	([3])	([3])	([3])	([3])	([3])
Total	−1	−48	−103	−198	−289	−358

[1] 18 to 20 years.
[2] Less than $5 million,
[3] Less than $1 million.
[4] Less than $10 million.

Table 4.—Revenue Effect of S. 2238 (Senator Hathaway): Amending the Carryover Basis Provisions of the Tax Reform Act of 1976

(millions of dollars)

Provision	Fiscal year— 1978	1979	1980	1981	1982	Long run [1]
Fresh start for losses	(3)	−10	−8	−5	−2	0
Minimum basis formula						
One "fresh start"						
Treat certain preferred stock as a marketable security	(2)	(2)	(2)	(2)	(2)	(2)
Increased minimum basis	(3)	−5	−16	−31	−50	−243
Single basis adjustment	(2)	(2)	(2)	(2)	(2)	(2)
Marginal rate basis adjustment	(3)	−4	−9	−16	−24	−109
Allocation of basis adjustment	(3)	+1	+3	+6	+7	+35
Value taxable gifts made within 3 years of death at time of transfer	(3)	(3)	(3)	(3)	(3)	(3)
Material participation rule for farm valuation	(3)	(3)	(3)	(3)	(3)	(3)
Closely held business definition	(3)	(3)	(3)	(3)	(3)	(3)
Total	(2)	−18	−30	−46	−69	−317

[1] 18–20 years.
[2] Less than $5 millon.
[3] Less than $1 million.

II. TREASURY PROPOSALS RELATING TO TECHNICAL AMENDMENTS

A. Estate and Gift Tax Provisions of H.R. 6715

1. Bond to Relieve Qualified Heir of Personal Liability for Recapture of Tax Where Special Use Valuation is Utilized (Sec. 3 (d)(5) of the bill and sec. 2032A of the Code)

Tax Reform Act of 1976

A qualified heir who receives property valued under the special use valuation provisions is personally liable for any additional tax arising from a disposition of the special use valuation property or the failure to use such property for a qualified use. As a condition precedent to a special use valuation election, *any person* with an interest in special use valuation property must agree in writing to be personally liable for the payment of any additional tax.

Technical Corrections Act

The bill provides that a qualified heir may be discharged from personal liability for payment of the additional tax upon filing a bond in the amount of the maximum amount of additional tax which could be attributed to such heir's interest in the property.

Issues

The required agreement may be a significant impediment to the practical utility of special use valuation. For example, a minor with a remainder interest in special use property is required to consent to personal liability for the payment of a tax which could arise through the action of another. The issue is whether the liability which arises through executing the required agreement should be discharged by a bond.

Proposed Treasury Amendment

The proposed amendment would extend this provision to all persons party to the required agreement.

Revenue Effect

This provision has no revenue effect.

2. Disclaimers (Sec. 3(m) of the bill and sec. 2518 of the Code)

Tax Reform Act of 1976

In order for a renunciation to constitute a qualified disclaimer, Code section 2518(b)(4) requires the disclaimed interest to pass to a person other than the person making the disclaimer.

Technical Corrections Act

The bill clarifies Code section 2518(b)(4) by providing that a disclaimer by any party (including a surviving spouse) will constitute a qualified disclaimer for purposes of Code section 2518 where the surviving spouse receives an interest in the disclaimed property.

98-286—77——4

Issue

The issue is whether a disclaiming party should be permitted to retain an interest in disclaimed property.

Proposed Treasury Amendment

The proposed amendment would make it clear that a qualified disclaimer will not result if, pursuant to the disclaimer, the disclaimed property passes to a trust or trust equivalent in which the disclaiming party has an interest.

However, an exception would apply to a surviving spouse who has received qualifying marital deduction property in amount within marital deduction limits, but which did not need to be qualified for the marital deduction because the unified credit would have exempted it from taxation anyway. Thus, the exception would apply to a surviving spouse who retains an interest in disclaimed property which qualified for the estate tax marital deduction in the estate of the decedent so long as the total amount of property which passed to the surviving spouse did not exceed the maximum estate tax marital deduction allowable to the estate of the decedent.

Revenue Effect

This provision has no revenue effect.

3. *Termination of Certain Powers of Independent Trustees Not Subject to Tax on Generation-Skipping Transfers (Sec. 3(n) (1) of the bill and sec. 2614 of the Code)*

Tax Reform Act of 1976

An individual trustee, other than a person whose only power over a trust is to dispose of trust income or corpus to beneficiaries who are lineal decedants of the grantor, is treated as a trust beneficiary for purposes of the generation-skipping tax.

Technical Corrections Act

The bill clarifies the situations in which an individual trustee having discretionary powers to allocate trust income and principal among beneficiaries will be treated as a beneficiary of such trust by reason of holding such powers. The bill provides that an individual trustee will not be treated as having power in a trust where such individual has no interest (including a future interest as a permissible appointee) in the trust, is not a related or subordinate trustee, and has no present or future power in the trust other than the power to dispose of trust income and corpus among beneficiaries designated in the trust instrument.

Issue

The issues involved are—

(1) Whether the definition of related or subordinate trustee should be expanded to cover other parties closely related to grantors and benficiaries; and

(2) whether trustees should be classified as beneficiaries solely because they may be permissible appointees under unexercised powers of appointment held by others.

Proposed Treasury Amendment

The proposed amendment would expand the definition of related or subordinate trustee to include (1) partners and employees of the grantor or of any beneficiary and (2) employees of any partnership in which the partnership interest of any of the grantor, the trust, or the beneficiaries of the trust are significant from the viewpoint of either operating control or distributive share of partnership income.

In addition to the definition of related or subordinate trustee would be confined to trustees who are members of generations younger than the grantor. Finally the definition of a beneficiary would be amended to exclude a permissible appointee under an unexercised power of appointment held by another.

Revenue Effect

This provision will increase budget receipts by a negligible aomunt.

4. Alternate Valuation Date in the Case of a Generation-Skipping Trust (Sec. 3(n)(3) of the bill and sec. 2602(d) of the Code)

Tax Reform Act of 1976

Code section 2602(d)(1) provides that the alternate valuation date will be available for generation-skipping transfers "from the same trust which have the same deemed transferor and which are taxable terminations occurring at the same time as the death of such deemed transferor."

Technical Corrections Act

The bill provides that the alternative valuation date will be available for taxable terminations postponed beyond the death of a single deemed transferor because of the existence of an older generation beneficiary at the death of the deemed transferor. The bill fails to cover another situation in which a taxable termination may be postponed and for which the alternate valuation date should be available.

Issue

Should the alternate valuation date be available also where a taxable termination is postponed beyond the death of a single deemed transferor because of the existence, at the death of the deemed transferor, of a beneficiary in the same generation as the deemed transferor?

Proposed Treasury Amendment

The proposed amendment would make the alternate valuation date available where a taxable termination is postponed beyond the death of a single deemed transferor because of the existence, at the death of the deemed transferor, of a beneficiary in the same generation as the deemed transferor.

Revenue Effect

This provision will increase budget receipts by a negligible amount.

5. Recapture in the Case of Satisfaction of a Pecuniary Bequest With Appreciated Carryover Basis Property (Sec. 2005(b) of the Tax Reform Act of 1976 and secs. 617, 1245, 1250, 1251, 1252 and 1254 of the Code)

Tax Reform Act of 1976

Code section 1040, added by the Tax Reform Act of 1976, provides that where appreciated property is used to satisfy a pecuniary bequest recognized gain will be limited to the difference between date of distribution and estate tax values. The purpose of Code section 1040 is to retain, under present law, the prior law income tax consequences of funding a pecuniary bequest with appreciated property. However, it is unclear whether recapture under Code sections 617, 1245, 1250, 1251, 1252 and 1254 is limited by the amount of gain recognized upon the satisfaction of a pecuniary bequest with appreciated carryover basis property.

Issue

The issue is whether Code sections 617, 1245(b), 1250(d), 1251(c), 1252 and 1254 should be amended to make clear that recapture is limited by the amount of recognized gain where appreciated carryover basis property is used to satisfy a pecuniary bequest.

Proposed Treasury Amendment

The proposed amendment provides that Code sections 617, 1245(b), 1250(d), 1251(c), 1252 and 1254 be amended to make clear that recapture is limited by the amount of recognized gain where appreciated carryover basis property is used to satisfy a pecuniary bequest.

B. Other Provisions

1. Disclosure of Returns and Return Information (Sec. 1202(a)(1) of the Tax Reform Act of 1976 and sec. 6103(k)(4) of the Code)

Tax Reform Act of 1976

Code section 6103(k)(4) exempts from the general disclosure rules of Code section 6103 the disclosure of tax return information to a competent authority of a foreign government "which has an *income* tax convention with the United States but only to the extent provided in . . . such convention." (Emphasis supplied.) The provision does not include estate and gift tax conventions and the Swiss Mutual Assistance Treaty, which have tax exchange of information provisions.

Issue

Should the exemption apply to estate or gift tax conventions and other agreements to exchange tax information?

Proposed Treasury Amendment

The proposed amendment would revise the exemption provided by Code section 6103(k)(4) to apply to a foreign government which has an income tax or an estate or gift tax convention or treaty with the United States. Also, the exemption would include a treaty such as the Swiss Mutual Assistance Treaty.

Revenue Effect

This provision would have no effect on budget receipts.

2. Contributions of Certain Government Publications (Sec. 2132 of the Tax Reform Act of 1976 and Sec. 1221(6) of the Code)

Prior Law

Under prior law, in most cases, Government publications received by taxpayers without charge (e.g., copies of the Congressional Record received by members of Congress) or at a reduced price were treated as capital assets. As a consequence of that treatment, those taxpayers were able to claim a reduction for the full fair market value of any such Government publications they contributed to a charity (such as a library or a university) for a use related to the charity's exempt purpose.

Tax Reform Act of 1976

The Act generally provided that U.S. Government publications received from the Government without charge or below the price at which they are sold to the general public are not to be treated as capital assets either in the hands of the taxpayer so receiving the publications or in the hands of a taxpayer whose basis in such a publication is determined by reference to its basis in the hands of a person who received it free or at a reduced price. However, because of a technical oversight, such publications were excluded from the definition of "capital asset" under section 1221 of the Code, but were not similarly excluded from the definition of "property used in the trade or business" under section 1231(b) of the Code. Because of this technical oversight, the Act fails to accomplish its intended purpose in respect of this issue.

Issue

The issue is whether the definition of "property used in the trade or business" under section 1231(b) of the Code should be amended to provide for the exclusion of U.S. Government publications which are received from the Government without charge or below the price at which they are sold to the general public from treatment as section 1231 assets.

Proposed Treasury Amendment

The amendment would amend section 1231(b) to provide that the term "property used in the trade or business" does not include U.S. Government publications received from the Government without charge or below the price at which they are sold to the general public.

Revenue Effect

This provision will cause a negligible increase in budget receipts.

III. OTHER PROPOSED AMENDMENTS

A. Income Tax and Administrative Provisions

1. Withholding of Federal Taxes on Certain Individuals Engaged in Fishing

Prior Law

Under the law prior to the Tax Reform Act of 1976, crewmen on boats taking fish or other forms of aquatic animal life were usually treated, for payroll tax purposes, as employees rather than self-employed individuals.

Tax Reform Act of 1976

Under the 1976 Act, crewmen on boats engaged in taking fish or other aquatic animal life with an operating crew of fewer than ten are to be treated as self-employed for Federal tax purposes if their sole remuneration is a share of the boat's catch (or the proceeds of the catch) or, in the case of an operation involving more than one boat, a share of the entire fleet's catch. Generally, the 1976 Act rule is applicable to services performed after December 31, 1971.

Issue

The issue is whether the provision of the 1976 Act be extended to services provided before December 31, 1971.

Proposed Amendment

The proposed amendment would extend the treatment for fishermen in the 1976 Act to all services performed after December 31, 1954.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Departmental Position

The Treasury Department supports this amendment.

2. Deduction for Attending Foreign Conventions

Prior Law

Prior to the 1976 Act, a deduction was allowed for traveling expenses paid or incurred to attend a foreign convention if the traveling expenses were reasonable and necessary in the conduct of the taxpayer's business and directly attributable to the trade or business. The lack of specific detailed requirements created substantial administrative problems for the IRS.

Tax Reform Act of 1976

The 1976 Act provided specific rules (sec. 274(h) of the Code) limiting the deduction for expenses of attending conventions, seminars or similar meetings held outside the United States, its possessions, and the

Trust Territory of the Pacific. These rules apply not only to the individual attending the convention, but also to his employer, where the employer pays the expenses.

Technical Corrections Act

The bill clarifies that the limitations added by the Tax Reform Act of 1976 on the deductibility of attending foreign conventions do not apply to an employer (or other person) paying the expenses of an individual attending a foreign convention (either directly or through reimbursement) where that individual is required to include the expenses in his gross income. This exception would not apply in any case where the amounts paid are not furnished by the payor on information returns or statements required to be furnished to the payee (i.e., Form W–2 or Form 1099).

Issue

The issue is whether there should be a requirement that a Form W–2 or Form 1099 must be filed in order for the employer (or other person) paying the expenses to be excepted from the foreign convention rules where the payments are includible in the payee's income.

Proposed Amendment

The proposed amendment would delete the requirement that a Form W–2 or Form 1099 be filed by the payor in order to be expected from the foreign convention limitations where the payments are includible in income by the individual attending a foreign convention. The proposal also corrects a technical drafting error.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Departmental Postion

The Treasury Department supports this amendment to the extent that it applies to situations where the person taking the deduction is not required under present law to file a Form W–2 or Form 1099. For example, in the case of a manufacturer who sends dealers' sales personnel on trips as a bonus for high sales, the manufacturer is not required, under present law, to file Forms W–2 and 1099 for the sales personnel. Rather, the dealer would be the employer required to file the forms. The Treasury Department would support the amendment to the extent that it would not require this manufacturer to file the forms as a prerequisite to taking the deduction. The Treasury Department understands that this is the intent of the sponsor, but points out that the draft language goes beyond this situation.

3. Accrual Accounting for Farm Corporations

Prior Law

Any taxpayer engaged in the trade or business of farming was entitled to use the cash method of accounting and to deduct currently costs which, for other businesses, would be included in inventory or capitalized.

Tax Reform Act of 1976

The 1976 Act requires generally that corporations engaged in farming use the accrual method of accounting and capitalize preproductive period expenses for taxable years beginning after December 31, 1976. Exceptions to these requirements were provided for (1) subchapter S corporations, (2) family corporations in which one family owns at least 50 percent of the stock, (3) nurseries, and (4) corporations with annual gross receipts of less than $1 million.

Tax Reduction and Simplification Act of 1977

This Act postponed the effective date of the accrual accounting provision until taxable years beginning after December 31, 1977, for any farm corporation in which either (a) two families own 65 percent of the stock or (b) three families own at least 50 percent of the stock and substantially all of the remaining stock is owned by employees and their families, or exempt pension (or similar) trusts for the benefit of the employees. This provision benefits Corbett Poultry Products Co. and Hudson Foods, etc.

Issue

The issue is whether the effective date of this provision should further be postponed for these corporations.

Proposed Amendment

The proposed amendment would postpone the effective date of the accrual accounting provision for an additional two years (until taxable years beginning after December 31, 1979) for farm corporations in which either (a) two families own at least 65 percent of the stock or (b) three families own at least 50 percent of the stock and substantially all of the remaining stock is owned by employees and their families, or exempt pension (or similar) trusts for the benefit of employees.

Revenue Effect

This provision will reduce budget receipts by less than $5 million per year.

Departmental Position

The Treasury Department opposes this amendment. The amendment was designed to benefit only two large poultry companies with annual receipts of at least $65 million each. It provides tax relief solely for large companies who can easily comply with the requirements because they have access to sophisticated accounting and recordkeeping procedures. In fact, these companies are already required to keep their financial records on the accrual basis to obtain certification of financial statements by an accountant. The current provisions already exempt from the accrual accounting requirement those corporations with gross receipts of $1 million or less which are over 93 percent of all farming corporations. If Congress believes that the subchapter S and "one-family" farm exceptions create inequities, the appropriate course of action would be to eliminate these exceptions, not to compound the inequities by enlarging the exceptions to encompass more businesses.

98-286—77——5

4. Negligence Penalty for Income Tax Preparers

Tax Reform Act of 1976

The Act established a negligence penalty of $100 per return for income tax return preparers who prepare a return containing an understatement of tax liability due to the "negligent or intentional disregard of IRS rules or regulations" of the Internal Revenue Service.

Issue

The Internal Revenue Service has proposed regulations stating that the term "rules and regulations" include Internal Revenue Service rulings. Thus, under the proposed regulations, disregard of an Internal Revenue Service ruling in certain situations (i.e., situations other than where the preparer in good faith believes that the ruling does not properly interpret the Code) may lead to a negligence penalty. The issue is whether the penalty should apply in this case.

Proposed Amendment

The amendment would require that in no case is the disregard of an Internal Revenue Service ruling to constitute a negligent or intentional disregard of Internal Revenue Service rules or regulations for purposes of the negligence penalty.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Departmental Position

The Treasury Department opposes this amendment.

5. Holding Period of Commodity Futures Contracts

Prior Law

Under prior law, assets were required to be held for more than 6 months to be eligible for long-term capital gain treatment.

Tax Reform Act of 1976

The 1976 Act increased the holding period for long-term capital gains to 9 months for 1977 and to 12 months for 1978 and subsequent years. An exception was provided for commodities futures contracts, which continue to be eligible for the 6-month holding period.

Technical Corrections Act

The bill limits the application of the 6-month holding period exception to agricultural commodity futures contracts.

Issue

The issue is whether the provision in the House-passed Technical Corrections Act limiting the exception to agricultural commodities futures contracts should be deleted so that the exception applies to all commodity futures contracts (including, for example, silver and other metals).

Proposed Amendment

The amendment would strike the provision in the Technical Corrections Act limiting the exception from the 9 and 12 months holding period to agricultural commodity futures contracts.

Revenue Effect

This provision will reduce budget receipts by $2 million in fiscal year 1978 and by $8 million for each fiscal year thereafter.

Departmental Position

The Treasury Department opposes this amendment. The pertinent committee reports in the 1976 Act refer only to "agricultural commodity futures contracts", although the Act did not include the term "agricultural." Treasury supports the Technical Corrections Bill—without amendment—because it corrects an error in the language of the 1976 Act and therefore carries out the intent of Congress to limit the exception of the increase of holding period rules to agricultural commodities futures contracts.

6. Rehabilitations of Historic Structures by Long-Term Lessees

Tax Reform Act of 1976

Under the 1976 Act, taxpayers are allowed to amortize over 5 years the expenses incurred in rehabilitating certified historic structures or, alternatively, to depreciate substantially rehabilitated historic structures using accelerated depreciation methods. It is not clear whether, or in what situations, the benefits of the 1976 Act provisions may be claimed by lessees who rehabilitate historic structures which they lease.

Technical Corrections Act

The bill makes several technical corrections to the historic structures provisions, but it does not determine whether lessees may claim rapid authorization deductions on expenditures incurred in rehabilitating leased historic structures.

Issue

The issue is whether long-term lessees should be permitted to claim rapid amortization deductions with respect to expenditures incurred in rehabilitating leased historic structures.

Proposed Amendment

The proposed amendment would permit lessees of historic structures to claim the rapid amortization deductions with respect to expenditures incurred in rehabilitating certified historic structures in situations where the lessee holds the historic structure under a lease which, at the time the improvements are made, has a remaining term at least as long as the useful life of the improvements (but in no event less than 30 years). As in the case of dispositions by owners of historic structures claiming the benefit of the 1976 Act provisions, benefits claimed by lessees under this proposal would be subject to recapture if the lease is terminated early.

Revenue Effect

This provision will reduce budget receipts by less than $5 million per year.

Departmental Position

The Treasury Department does not oppose this provision if (1) it is limited to historic structures owned by governments or exempt organizations, and (2) it is limited to structures that are "certified historic structures" because they are either listed in the National Register or located in a district listed in the National Register.

7. Basis of Player Contracts Acquired in Connection with The Acquisition of a Sports Franchise

Prior Law

Under prior law, there was no specific rule relating to the allocation of a portion of the total consideration paid to acquire a sports franchise, including players' contracts and other assets which might be acquired at the time of acquisition of a franchise. Generally, this allocation was made on the basis of the estimated fair market values (or relative fair market values) of the various assets.

Tax Reform Act of 1976

The Act provides that, in the case of the sale, exchange or other disposition of a sports franchise (or the creation of a new franchise), the amount of consideration allocated to a player contract by the transferee shall not exceed the sum of the adjusted basis of the contract in the hands of the transferor immediately before the transfer and the gain (if any) recognized by the transferor on the transfer of the player contract.

The Act also provides that, in the case of the sale or exchange of a sports franchise, it is presumed that not more than 50 percent of the consideration is allocable to player contracts unless the taxpayer can satisfy the Secretary of the Treasury that under the facts and circumstances of the particular case, it is proper to allocate an amount in excess of 50 percent.

The provision relating to the allocation of basis to player contracts applies to sales or exchanges of franchises after December 31, 1975, in taxable years ending after that date.

Issue

The issue is whether the basis allocation limitation rules should apply to a taxable merger occurring after December 31, 1975, if financing for purchasing certain shareholders' interests had been arranged on November 7, 1975, and a proposed proxy statement with respect to the merger had been submitted to the Securities and Exchange Commission before September 21, 1976.

Proposed Amendment

The proposed amendment would provide an exception to the basis allocation rules adopted by the 1976 Act be provided with respect to property acquired by the transferee in a taxable merger if a proposed proxy was submitted to the Securities and Exchange Commission before September 21, 1976.

The amendment would benefit Mr. William H. Sullivan, Jr., and the New Patriots Football Club, Inc.

Revenue Effect

This provision will reduce budget receipts by between \$2 and \$3 million over a period of 4–6 years.

Departmental Position

The Treasury Department opposes this amendment.

8. Special Recapture Rules for Depreciation on Player Contracts

Prior law

Prior to the 1976 Act, in the case of a sports franchise, the amount of the cost attributable to a player's contract which was depreciated over the useful life of the contract was recaptured as ordinary income on a contract-by-contract basis. Thus, a substantial amount of depreciation allowed with respect to player contracts was never recaptured as ordinary income since many of the original players had retired or been "cut" by the time the franchise was subsequently sold.

Tax Reform Act of 1976

The 1976 Act provided a special rule for the recapture of depreciation for losses taken with respect to player contracts in the case of the sale or exchange of the entire sports franchise occurring after December 31, 1975. In general, rather than determining recapture on a contract-by-contract basis, this rule provides for recapture of depreciation taken with respect to player contracts on a consolidated basis. Thus, the amount of depreciation recapture "pool" generally will include depreciation on player contracts acquired with the franchise even though the individual player has retired by the time of subsequent sale of the sports franchise. Under the House bill, this special recapture rule applied only in the case of post-1975 depreciation. Under the Senate bill (and the provision adopted in conference), the special rule was extended to recapture both pre-1976 and post-1975 depreciation in the case of sales or exchanges occurring after December 31, 1975.

Issue

The issue is whether the special "pool" recapture rules should apply to depreciation allowed on player contracts prior to January 1, 1976.

Proposed Amendment

The proposed amendment would provide that only depreciation allowable after December 31, 1975, would be subject to the special recapture rules. Depreciation on player contracts prior to January 1, 1976, would be subject to the recapture rules in effect prior to the changes made by the 1976 Act (i.e., recapture on a contract-by-contract basis.

The proposed amendment would apply generally to all sports franchises with respect to the recapture of pre-1976 depreciation. With respect to specific transactions, the amendment would apply to the sale of the Atlanta Braves by the Atlanta/LaSalle Corporation in January 1976.

Revenue Effect

This provision will reduce budget receipts by $1 million in fiscal 1978 and by negligible amounts thereafter.

Departmental Position

The Treasury Department supports this amendment.

9. Securities Lending

Present Law

Exempt organizations—unrelated business income.—The investment income of exempt organizations generally is not subject to the tax on unrelated business income. The types of investment income sources listed as being generally free of this tax are dividends, interest, annuities, royalties, rents, and capital gains from the sale of investment assets (sec. 512(b) (1), (2), (3), and (5)). An organization may be treated as a public charity (i.e., not a private foundation) if the organization normally receives not more than one-third of its support from gross investment income plus the excess of the organization's unrelated business taxable income over the amount of the tax imposed on such income (sec. 509(a) (2)). The term "gross investment income" does not include any income to the extent included in computing the unrelated business income tax.

Regulated investment companies.—For a corporation to qualify as a regulated investment company, at least 90 percent of its gross income must be derived from dividends, interests, and gains from the sale or other disposition of stock or securities (sec. 851(b) (2)).

Because of time delays which a securities broker may face in obtaining securities to deliver to a purchaser (from the seller), brokers frequently borrow securities from organizations with investment portfolios, including exempt organizations and regulated investment companies. In general, the lender of securities is compensated for the loan in two ways. First, if a dividend or interest is paid with respect to the security during the term of the loan, the borrower pays the lender an amount equal to that dividend or interest payment. Second, a fee is paid for the use of the security.

The Internal Revenue Service has ruled privately that payments on securities loans are not dividends or interest even if they are paid by the broker (borrower) as the equivalent of a dividend or interest payment on the underlying security.

Issue

The issue is whether, where the loan is fully collateralized in accordance with the Securities and Exchange Commission requirements, the income from the lending of a security should be regarded as investment income (similar to dividends and interest) in the case of exempt organizations and regulated investment companies.

Proposed Amendment

The amendment provides, in general, that payments in respect to securities loans which satisfy certain requirements are to be treated in the same manner as dividends and interest in the case of a lender which is an exempt organization or a regulated investment company.

Effective Date

This amendment applies to amounts received after December 31, 1976, regardless of whether the organization involved is a calendar year taxpayer or a fiscal year taxpayer.

Prior Congressional Action

An identical provision (except for the effective date) was approved by the Finance Committee last year as an amendment to H.R. 7929. It was deleted from that bill on October 1, 1976 (the last day of the 94th Congress) to enable H.R. 7929 to be enacted without a House-Senate conference.

Revenue Effect

This provision will reduce budget receipts by less than $5 million per year.

Departmental Position

To the extent this issue involves exempt organizations, the Treasury Department states that the program has been acceptably resolved at the administrative level and no legislation is necessary. Treasury does not oppose that portion of the proposed legislation which specifically relates to regulated investment companies.

10. Personal Holding Companies—Definition of "Individual" for Stock Ownership Test

Prior Law

Under the Code, a tax is imposed on the undistributed income of a "personal holding company." Basically, a "personal holding company" is a corporation which derives most of its income from certain passive sources and 50 percent or more of whose stock is owned by 5 or fewer individuals.

Prior to the Tax Reform Act of 1976, an organization or trust organized or created before July 1, 1950, would not be counted as an individual in determining whether a corporation constituted a personal holding company if the organization or trust owned all of the common stock and at least 80 percent of the other stock of the corporation.

Tax Reform Act of 1976

The Tax Reform Act of 1976 deleted this last exception as part of the "deadwood" provisions of that Act because it was believed that all such organizations would have been liquidated by that time.

Issue

It has come to the attention of the staff that at least one company still comes within the provision eliminated under the deadwood provisions. That company is the E. L. Pomar Investment Company which is owned by the E. L. Pomar Foundation of Colorado Springs, Colorado. The issue is whether the exception in prior law should be reinserted into the law.

Proposed Amendment

The proposed amendment would reinsert the provision of prior law that was deleted by the deadwood provisions of the 1976 Act.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Department Position

The Treasury Department has no objection to this amendment in principle. However, the amendment should change the effective date of the deletion of the deadwood provision rather than reinsert the exception in prior law.

11. Shareholder Rules For Subchapter S Corporations

Prior law

The subchapter S rules allow certain corporations engaged in an active trade or business to elect to be treated for income tax purposes in a manner similar to a partnership. A corporation which has its subchapter S election terminated or revoked may not make a new election until the sixth taxable year after the prior election was in effect. Under prior law, one of the requirements for electing subchapter S treatment was that the corporation have 10 or fewer shareholders.

Tax Reform Act of 1976

The Act increased the number of shareholders permitted in a subchapter S corporation to 15 after the corporation has been an electing subchapter S corporation for five consecutive years. In situations where a corporation had been under a subchapter S election for five consecutive years and this election was terminated or revoked, the legislative history of the amendment did not require that the 5-year rule be satisfied again in order to have more than 10 shareholders under a new election. However, it was required that the corporation have, in fact, more than 10 shareholders at the end of its previous election in order to avoid application of the 5-year rule under the new subchapter S election.

Issue

The issue is whether a corporation which makes a new subshapter S election must have had more than 10 shareholders on the last day of the last taxable year covered by the previous election.

Proposed Amendment

The amendment would provide that a corporation which was previously under a subchapter S election for five consecutive years may make a new election, and immediately have the new shareholder limits apply.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Departmental Position

The Treasury Department prefers a uniform 15 shareholder limit rather than complex conditions on increasing the limit from 10 to 15.

12. Certain Income of Howeowners Associations

Tax Reform Act of 1976

The Act provides that certain condominium management associations or residential real estate management associations may elect to be treated as tax-exempt organizations. If an election is made, the association is not taxed on membership dues, fees and assessments received from members of the association who own residential units in the particular condominium or subdivision (called "exempt function income").

However, the association is to be taxed as a corporation (without the surtax exemption) on other income, including investment income and income derived from a trade or business. Deductions are allowed for expenses directly related to the production of nonexempt income, and a $100 deduction against nonexempt income is provided so that associations with only a minimal amount of otherwise taxable income will not be subject to tax.

Issue

The issue is whether the exemption for housing associations should be extended to income derived by the housing association from the efforts of its members or from the sale of goods contributed to the housing associations.

Proposed Amendment

The proposed amendment would broaden the definition of "exempt function income" for homeowners associations to include (1) income from a trade or business in which substantially all the work in carrying on that trade or business is performed without compensation and (2) income from selling merchandise, substantially all of which has been received as gifts.

Revenue Effect

This provision will reduce budget receipts by less than $5 million per year.

Departmental Position

The Treasury Department opposes this provision in principle. However, the Treasury does not object to a rule which would exempt a de minimus amount of this type of income, for example, $1,000 for accounting convenience.

13. Reduction of Private Foundation Excise Tax Based on Investment Income

Present law

The Tax Reform Act of 1969 imposed a 4-percent excise tax upon the net investment income of private foundations (sec. 4940).

At the time of the Tax Reform Act of 1969, the Finance Committee concluded that it was appropriate to impose a tax on private foundations in the nature of an audit fee to cover the cost of the Internal Revenue Service's administration of the tax laws pertaining to exempt organizations. The Committee thus concluded that private foundations should not be required to pay taxes at such a level as to be contributing to the general revenues. Since the tax became effective in 1970, the revenues raised by section 4940 have been at least double the cost of supervising all exempt organizations.

Issue

Should the excise tax on investment income of private foundations be reduced to reflect the cost to the Internal Revenue Service of administering the tax laws pertaining to exempt organizations.

Proposed Amendment

The proposed amendment would reduce the rate of tax on investment income of private foundations from 4 percent to 2 percent.

Other Congressional Action

A similar provision was included in the Senate's version of the Tax Reform Act of 1976, but it was deleted in conference. The House

Ways and Means Committee has recently ordered reported a bill (H.R. 112) which would reduce this tax rate to 2 percent, but the bill has not yet been reported.

Revenue Effect

This provision will reduce fiscal budget receipts by $27 million per year.

Departmental Position

The Treasury Department supports this amendment.

14. Mutual Deposit Guaranty Funds

Present Law

Under present law, certain nonprofit mutual associations that are formed to provide guaranty funds for savings and loan associations, cooperative banks, and mutual savings banks are exempt from Federal income tax (sec. 501(c)(14)). However, in order to qualify for the exemption, the organization must have been created before September 1, 1957.

Issue

The issue is whether the exemption should be extended to organizations created after September 1, 1957, and, if so, should the change be made retroactively.

Proposed Amendment

The proposed amendment would permit mutual deposit guaranty funds which are created before January 1, 1963, to be exempt. The exemption would be retroactively granted to taxable years beginning after December 31, 1974. This change would primarily benefit the Maryland Savings-Share Insurance Corporation.

Prior Congressional Action

In 1976, an amendment was approved on the Senate floor extending exemption to associations created before January 1, 1969, and to organizations created before that date which insure both credit unions and savings and loan associations. This floor amendment, which would have benefitted three organizations (one in Maryland, one in North Carolina, and one in Massachusetts), was deleted in conference.

Revenue Effect

This provision will reduce budget receipts by $2 million in fiscal 1978, and by less than $1 million per year thereafter.

Departmental Position

The Treasury Department opposes this amendment. Congress made the basic decision 20 years ago to tax these private organizations. It provided relief to existing organizations by grandfathering them. There is no reason to change this decision. In addition, Treasury suggests that the permanent grandfather exemption be removed after 5 years.

15. Retroactive Election for Individuals Married to Nonresident Aliens to File Joint Returns

Prior Law

Under prior law, a joint return could not be filed if either the husband or wife was, at any time during the taxable year, a nonresident alien. In addition, since married taxpayers are not eligible for the 50-percent maximum tax on earned income unless they file a joint return, taxpayers married to nonresident aliens could not qualify for the maximum tax.

Tax Reform Act of 1976

The 1976 Act allows citizens and residents married to nonresident aliens to file joint returns provided that both spouses elect to be taxed on their worldwide income. Taxpayers making the election to file joint returns will be eligible for the maximum tax. The election for nonresident spouses to be treated as U.S. residents applies to taxable years ending on or after December 31, 1975.

Technical Corrections Act

The bill makes several technical corrections to the provisions allowing individuals married to nonresident aliens to file joint returns, but it does not make any changes to the effective date of the provision.

Issue

Should the election permitting U.S. residents or citizens married to nonresident aliens to file joint returns be made effective for years prior to 1975.

Proposed Amendment

The proposed amendment would permit residents or citizens married to nonresident aliens to make a retroactive election to file joint returns for all years (open or closed) beginning after 1969.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Departmental Position

The Treasury Department opposes this amendment. Treasury states that they have supported the election prospectively, but are generally opposed to this type of retroactive amendment. The Congress carefully considered the effective date in its deliberations on the 1976 Act. It is undesirable to provide a retroactive effective date because virtually all the tax returns have been filed. The inequitable consequence is that only those taxpayers who are aware of the change and file amended returns will obtain the benefits. Furthermore, the change would generate many amended returns. Processing these returns, as well as informing the public of the option to file the returns, places significant burdens on the Internal Revenue Service.

16. Treatment of ESOP Investment Credit Under the Minimum Tax

Prior Law

The minimum tax applies to items of tax preference at a 10-percent rate with an exemption equal to $30,000 plus the amount of the regular taxes paid.

Tax Reform Act of 1976

The Act increased the minimum tax rate to 15 percent and modified the exemption, in the case of individuals, to the greater of $10,000 or one-half of regular taxes paid and, in the case of corporations, to the greater of $10,000 or total regular taxes paid.

A taxpayer's regular tax liability is reduced by various deductions and credits, including the 1 or 1½ percent additional investment credit for contributions to Employee Stock Ownership Plans (ESOP). The reduction in taxes for the ESOP investment credit, in turn, reduces the exemption from the minimum tax for regular taxes paid, which increases the amount of preferences on which some minimum tax must be paid.

Issue

The issue is whether the amount of regular taxes paid for purposes of the minimum tax should be considered to include the ESOP investment credit allowable.

Proposed Amendment

The amendment provides that the amount of regular taxes which are allowed to offset minimum tax preferences is not to be reduced by the amount of any investment tax credit for contributions to Employee Stock Ownership Plans.

Revenue Effect

This provision will reduce budget receipts by $1 million per year.

Departmental Position

The Treasury Department opposes this amendment.

17. Lump-Sum Distributions From Investment Credit ESOPs

Present Law

ERISA provides that in order for a distribution to an employee from a qualified plan to be eligible for 10-year income averaging applicable to lump-sum distributions, the total interest of the employee under the plan and under all comparable plans maintained by the employer must be distributed to him in one taxable year. Under present law, an employer is granted a higher investment credit if an ESOP is established. If there is an early disposition of the property, all or a portion of the investment credit is recaptured.

Issue

The issue is whether an employee who is covered by an investment credit ESOP as well as by a comparable tax-qualified plan maintained by his employer should be eligible for 10-year income averaging upon a distribution of all of his benefits under both plans where an amount is retained of his benefits under both plans where an amount is retained by the investment credit ESOP as a reserve against recapture of investment credit previously contributed to the ESOP.

Proposed Amendment

Under the proposed amendment, a distribution to an employee from a qualified plan otherwise eligible for 10-year income averaging will not become ineligible solely because a portion of the employee's interest in an investment credit ESOP maintained by the same employer is retained by the investment credit ESOP to permit recovery by the employer of recaptured investment credit.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Departmental Position

The Treasury Department does not support this amendment, because it adds complexity to the already complex investment credit ESOP provisions without a concomitant benefit to those taxpayer who maintain these plans.

18. Expiring Investment Credit Carryovers

Prior Law

In general, investment credits can offset $25,000 plus 50 percent of tax liability beyond $25,000. Credits not used in the current year can be carried back for 3 years or forward for 7 years.

Tax Reform Act of 1976

The Act generally applied a first-in-first-out treatment of investment credits, under which credits arising from earlier years are applied to the current year's tax liability before any credits arising in the current year. In addition, the Act established a temporary 100-percent limit on the amount of regular tax liability of railroads and airlines which could be offset by investment tax credits.

Issue

The issue is whether or not credits for which there is a 10-year carryover under present law, but which otherwise would expire in 1977 for airlines, should be carried forward one additional year in cases where prior net operating losses have prevented their use.

Proposed Amendment

The amendment would allow an additional one-year carryover for investment tax credits which would otherwise expire at the end of 1977 in the case of credits from airline property which could not be used in earlier years because of net operating losses. The amendment would benefit Texas International Airlines, and possibly other air carriers in a comparable position.

Revenue Effect

It is estimated that the total amount of expiring investment credits of airlines for 1977 is at least $50 million. However, since most airlines have investment credits from other years which could be used in 1978 in any case, the revenue reduction from the amendment could be as little as $1 million in fiscal 1978 and $1 million in fiscal 1979. The remaining credits could result in a reduction of revenues in later fiscal years.

Departmental Position

The Treasury Department opposes this amendment. Under present law, these taxpayers have a benefit not extended to other taxpayers because they can use the credit up to 100 percent of tax liability. In addition, the 10-year carry-over of pre-1971 credits under present law is longer than the time permitted for credits in current years. Time periods for carryback and carryover provisions must be subject to definite limits. An extension would require the Internal Revenue Service to examine 14 years of tax returns to determine the appropriateness of the use of the credit. The lengthy time period and 100 percent offset already provide generous relief for these taxpayers and place a burden on the Service. The time period should not be extended further.

19. Treatment of Partnership Liabilities Where a Partner Is Not Personally Liable

Prior Law

Under prior law, a partner was able to deduct his distributive share of all the deductible items of the partnership, but the total amount of the deductions was limited to the amount of the adjusted basis of his interest in the partnership. Under the income tax regulations in effect under prior law, a partner's adjusted basis in his partnership interest was increased by a portion of any partnership liability with respect to which there was no personal liability on the part of any of the partners (Treas. Reg. § 1.752–1(e)). This rule enabled partners to deduct amounts for tax purposes exceeding the amount of investment that they had economically at risk in the partnership.

Tax Reform Act of 1976

The 1976 Act provided that, in general, for purposes of the limitation on allowance of partnership losses, the adjusted basis of a partner's interest would not include any portion of any partnership liability with respect to which the partner has no personal liability. However, two exceptions to this rule were provided. Under the first exception, the rule did not apply with respect to any activity to the extent that the specific at risk rule (sec. 465) applied. Under the second exception, the rule did not apply to "any partnership the principal activity of which is investing in real property (other than mineral property)". This second exception has created considerable difficulty because of ambiguities in the terms "investing" and "principal activity".

Technical Corrections Act

The bill provides that the real property exception applies where "substantially all" of the activities of the partnership relate to the holding of real property (other than mineral property) for sale or rental.

Issue

The issue is whether qualification for the real property exception to the limitation on loss rule should apply only to the extent of the aggregate amount of any nonrecourse partnership liability incurred in connection with the purchase, contribution to the partnership of, or improvement to, any real property owned by the partnership, but not in excess of the fair market value of the real property (or properties) subject to the nonrecourse liability at the time the liability is incurred.

Another issue is whether the losses attributable to any partnership activity other than one using the real estate subject to the nonrecourse liability should be deductible against basis attributable to nonrecourse liabilities on real property.

Proposed Amendment

The amendment would clarify these ambiguities by providing that this exception would apply to the extent of the aggregate amount of its nonrecourse liabilities incurred in connection with the acquisition of, or improvement of, any real estate owned by the partnership, but only to the extent of the fair market value of the real property.

In addition, the proposed amendment would not allow partnership losses from activities which are totally unrelated to the activity or activities in which the real property is used to be deductible by a partner to the extent his basis in the partnership is attributable to nonrecourse liabilities on the partnership real property. As under present law, the proposed amendment also does not allow basis attributable to nonrecourse liabilities on real property to be used to support deductions from farming, equipment leasing, or oil and gas activities which are subject to the specific at risk rules of section 465.

Revenue Effect

This provision will reduce budget receipts by less than $5 million per year.

Departmental Position

The Treasury Department agrees that the present exception for real estate from the partnership at-risk rule is ambiguous. Treasury states that they prefer the approach of the House bill (H.R. 6715) which would except only a partnership "substantially all of the activities of which relate to the holding of real property (other than mineral property) for sale or rental", since Treasury believes it would be easier to administer than the proposed amendment. However, Treasury recognizes that he House bill may not be broad enough to cover all cases intended to be within the exception. Therefore, Treasury does not object to the amendment provided there are sufficient safeguards to prevent basis from nonrecourse financing on real estate to be utilized to deduct losses which have only a minimum or indirect connection with the real estate.

20. Exemption From At-Risk Limitation for Certain Leasing Activities

Tax Reform Act of 1976

Under the Tax Reform Act of 1976, the amount of any loss (otherwise allowable for the year) which may be deducted in connection with certain activities, including equipment leasing, cannot exceed the aggregate amount with respect to which the taxpayer is at risk in each such activity at the close of the taxable year. The limitation applies to all taxpayers other than corporations which are not subchapter S corporations or personal holding companies.

Issue

Should the at-risk limitation be applied to taxpayers who lease office furniture, fixtures or equipment where the taxpayer actually participates in the management of that leasing business.

Proposed Amendment

The proposed amendment provides that the at-risk limitation does not apply to a small business concern or a subchapter S corporation to the extent that it is engaged in the leasing of office furniture, fixtures and equipment where the taxpayer actively participates in the management of that concern or corporation.

Revenue Effect

This provision will reduce budget receipts by $9 million in fiscal years 1978 and 1979, and by $7 million per year thereafter.

Departmental Position

The Treasury Department opposes the amendment. Treasury indicates that they are currently studying the application of the at-risk provisions to regular business corporations generally and their effect on taxpayers, such as those affected by the amendment. Also, Treasury believes that the amendment may cause difficult interpretative problems (ie., what is active participation in management), which might make it difficult to limit its scope to nontax shelter arrangements. Treasury notes that amendment will not apply unless there is a combination of nonrecourse financing, tax losses from the leasing activity and unrelated income to be offset by the losses.

21. Limitations on Profit-Sharing Benefits and Contributions

Employee Retirement Income Security Act of 1974 (ERISA)

Under ERISA the annual addition to the account of a participant in a tax-qualified profit-sharing plan may not exceed the lesser of (a) $25,000 (plus cost-of-living increases) or (b) 25 percent of the participant's annual compensation.

Issue

Where employer contributions to a profit-sharing plan are allocated to employees on a per capita or hour-of-service basis, the sole effect of the 25-percent limitation may be to restrict allocations for part-time or other low-paid workers.

The issue is whether the percentage limitation should apply to a participant in a profit-sharing or other defined contribution plan if contributions are based solely on a per capita or hours-of-service formula.

Proposed Amendment

Under the proposed amendment, the 25-percent-of-compensation limitation would not apply to a participant in a profit-sharing or other defined contribution plan which bases contributions solely on a per capita or hours-of-service formula. The limitations would continue to apply, however, with respect to participants who are officers, shareholders, highly compensated employees or self-employed individuals.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Departmental Position

In general, the Treasury Department supports this amendment, because it encourages a pension plan to make proportionately greater contributions to lower paid persons. However, Treasury believes the amendment should be modified so that contributions generally could not be based on hours of service. Rather, the plan should be permitted to prorate contributions, based on hours of service, only for those persons completing less than 2,000 hours of service, as permitted by ERISA.

In addition, to assure that contributions in excess of 25% of compensation are not made for highly compensated persons, this exception from the general rules should apply only to a plan under which no more than one-third of the employer contributions are allocated to a group consisting of officers, 10 percent shareholders, and highly-paid employees, as is provided for ESOPs under current law.

22. Source of Income on Redemption of Stock in Foreign Corporation

Prior Law

The source of income derived from the sale of personal property, including stock, is generally determined by the place where the sale or exchange of stock occurred. Thus, gain recognized on the redemption of stock in a foreign corporation was treated as income from sources within the country in which the foreign corporation was incorporated.

Tax Reform Act of 1976

The 1976 Act provided as a general rule that gain on the sale or exchange of personal property outside the United States (including redemptions of stock in foreign corporations) which is not subject to a foreign tax of at least 10 percent will not be considered foreign source income. That general rule does not apply to certain specified situations including, in the case of a sale or exchange by a corporation of stock in a second corporation, those where the stock is sold in a country in which the second corporation derived more than 50 percent of its gross income. The provision was intended to prevent taxpayers from maximizing the use of foreign tax credits by arranging for sales of personal property to take place in low-tax foreign countries.

Technical Corrections Act

The bill contains no provision modifying the 1976 Act provisions in the case of redemptions. However, in the case of income received by a corporation on the liquidation of a foreign corporation, the bill modifies the 1976 Act rule to provide that income will be treated as from foreign sources in all cases where the foreign corporation derives most of its income from foreign sources. This modification was made because the potential for artificially arranging a sale in a low-tax country does not exist in the case of liquidations because under the normal source rules any gain from a liquidation has a source in the country of incorporation.

Issue

Since the potential for artificially arranging of a sale in a low-tax country also does not exist in the case of redemptions, should the provision in the bill treating gain on liquidations as foreign source income be expanded to apply also to gain on the redemption of stock of foreign corporation.

Proposed Amendment

The proposed amendment would treat gain received by a corporation on the redemption of stock in a foreign corporation as foreign source income in all cases where the foreign corporation derives most of its income from foreign sources. The proposed amendment is intended to benefit the Armco Steel Corporation.

Revenue Effect

It is estimated that this amendment will decrease revenues by approximately $10 million in fiscal 1978 and by less than $5 million per year thereafter.

Departmental Position

The Treasury Department would support this amendment which treats redemption proceeds as foreign source income in these circumstances *if*, *but only if*, the section 904 limitation were to be applied separately with respect to capital gains (in the same manner that the limitation is applied separately, under section 904(d), for interest income and DISC dividends).

23. Inspection by Committees of Congress of Exempt Organization Information Available to the Public

Tax Reform Act of 1976

The 1976 Act substantially revised the rules relating to the confidentiality of returns and return information. However, the 1976 Act failed to correct a technical problem existing under section 6104 of the Code with respect to disclosure of certain exempt organization information to committees of Congress.

In general, section 6104 makes available to the public certain applications and other documents relating to the qualification of tax-exempt organizations and pension, profit-sharing, and stock bonus plans. However, this section further provides that these applications and documents are only available to committees of Congress pursuant to a more stringent disclosure provision found under section 6103.

Issue

The issue is whether committees of Congress should be able to obtain applications and other documents relating to qualification of tax-exempt organizations and pension, profit-sharing, and stock bonus plans on the same basis as the public.

Proposed Amendment

The amendment would provide that those applications and related documents which are made available to the public under section 6104 would also be made available on the same basis for inspection by committees of Congress.

Effective Date

The amendment made by this provision would be effective January 1, 1978.

Revenue Effect

This provision has no effect on budget receipts.

Departmental Position

The Treasury Department supports this amendment.

24. Travel Expenses of State Legislators

Present law

Under present law, an individual is allowed a deduction for traveling expenses (including amounts expended for meals and lodging) while away from home in the pursuit of a trade or business (sec. 162 (a)).

A taxpayer's "home" for purposes of the deduction for traveling expenses generally means his principal place of business or employment. If a taxpayer has more than one trade or business, or a single trade or business which requires him to spend a substantial amount of time at two or more localities, his tax "home" is held to be at his principal place of business. A taxpayer's principal place of business is determined on an objective basis taking into account the facts and circumstances in each case. The more important factors to be considered in determining the taxpayer's principal place of business (or tax home) are: (1) the total time ordinarily spent by the taxpayer at each of his business posts, (2) the degree of business activity at each location, (3) the amount of income derived from each location, and (4) other significant contacts of the taxpayer at each location. No one factor is determinative.

In 1952, a provision was adopted with respect to the living expenses paid or incurred by a Member of Congress (including a Delegate or Resident Commissioner). Under these rules, the place of residence of a Member of Congress within the congressional district which he represents in Congress is considered his tax home. However, amounts expended by the Member within each taxable year for living expenses away from home are not deductible in excess of $3,000. Therefore, a Member of Congress (who does not commute on a daily basis from his congressional district) can deduct up to $3,000 of his expenses of living in the Washington, D.C. area. Prior to the Tax Reform Act of 1976, no rule similar to the special rules for ascertaining the place of residence for a Member of Congress applied in the case of a State legislator. As a result, the tax home of a State legislator was determined in accordance with the general rules described above.

Tax Reform Act of 1976

The Tax Reform Act of 1976 provided an election for the tax treatment of State legislators for taxable years beginning before January 1, 1976 for which the period of assessing or collecting a deficiency had not expired prior to the date of enactment. Under this election, a State legislator may, for any such taxable year, treat his place of residence within his legislative district as his tax home for purposes of computing the deduction for living expenses. If this election was made, the legislator was treated as having expended for living expenses an amount equal to the sum of the daily amount of per diem generally allowed to employees of the U.S. Government for traveling away from home, multiplied by the number of days during that year that the State legislature was in session. For this purpose, the number of days taken into account included any day in which the legislature was in recess for a period of 4 or fewer consecutive days. In addition, if the State legislature was in recess for more than 4 consecutive days, a State legislator could count each day in which his physical presence was formally recorded at a meeting of a committee of the State legislature. For this purpose, the rate of per diem to be used was the rate that was in effect during the period for which the deduction was claimed. No substantiation of the amount of such expenses was required.

Tax Reduction and Simplification Act of 1977

The Tax Reduction and Simplification Act of 1977 extended this election to taxable years beginning before January 1, 1977.

Issue

The issue is whether the election made available by the Tax Reform Act of 1976 for a State legislator to treat his residence within his legislative district as his home for purposes of determining his deductible travel expenses should be extended to taxable years beginning in 1977.

Proposed Amendment

The amendment extends the election for State legislators to taxable years beginning before January 1, 1978.

Revenue Effect

This provision will reduce budget receipts by less than $5 million in fiscal year 1978.

Departmental Position

The Treasury Department has no objection to this amendment.

25. Awards Under the Public Health Services Act

Present law

In Revenue Ruling 77-319, the Internal Revenue Service ruled that amounts received as National Research Services Awards (NRSA), under the Public Health Service Act of 1974 [1] are not excludable scholarships or fellowship grants under section 117 of the Code.

In return for an NRSA award, the recipient must engage in health research or teaching or some equivalent service and also must allow the Government royalty-free use of any copyrighted materials produced as a result of research performed during the award period. Within two years after the award period, a recipent must engage in health research or teaching or in some other service designated by the Secretary of Health, Education and Welfare for a period equal to the award period. If a recipient fails to complete the post-award service requirements, he must repay an amount determined under a formula which takes into account the amount of the award, the length of the service obligation, and any actual post-award service.

Postdoctoral awards generally range between $10.000 and $14,000 annually and usually do not exceed three years. Either type of award may be supplemented by non-Federal funds and by explicity authorized Federal funds from other programs.

The IRS ruled that the NRSA awards to not qualify as excludable scholarships or fellowship grants for two principal reasons: (1) the post-award service requirement imposes a substantial *quid pro quo* for

[1] Public Law 93-348, secs. 472 and 473, as amended.

the award and (2) the Government's interest in maintaining biomedical and behavioral research and its royalty-free right to materials produced as a result of research performed during the award period indicate that the awards are not disinterested, "no-strings" educational grants but instead are made primarily for the benefit of the grantor (the Government).

Issue

The issue is whether National Research Service Awards, granted by the Federal Government for biomedical and behavioral research, should be included in income and subject to Federal income taxation.

Proposed Amendment

The amendment provides that National Research Service Awards, received under sections 472 and 473 of the Public Health Services Act of 1974, as amended, are to be treated as a scholarship under section 117 of the Internal Revenue Code and, thus, excluded from gross income. The amendment applies to amounts received pursuant to awards made after January 1, 1974, and before January 1, 1979.

Revenue Effect

This provision will reduce budget receipts by $35 million in fiscal 1978 and by $17 million in fiscal 1979.

Departmental Position

The Treasury Department has no objection to this amendment.

B. Carryover Basis and Estate and Gift Tax Provisions

1. Carryover Basis and Corporate Buyout Agreements

Prior Law

Under the present law (sec. 101 of the Code), the transfer of a life insurance policy for a valuable consideration will result in a reduction in the portion of the policy's death proceeds that will be excludable from the recipient's gross income.

For valid business reasons, closely-held corporations frequently utilize buyout arrangements. Such arrangements, which are usually funded with life insurance on the lives of the shareholders, may be in the form of a stock-redemption agreement or a cross-purchase agreement. In a stock-redemption agreement, the life insurance is held by the corporation. At the death of a shareholder, the corporation uses the proceeds of the life insurance to redeem the stock of the deceased shareholder. In a cross-purchase agreement, the life insurance is held by the other shareholders. At the death of a shareholder, the other shareholders use the proceeds of the life insurance to purchase the stock from the deceased shareholder's estate.

Under prior law, the basis of the stock to the heirs of the surviving shareholders was the same under either arrangement because the basis of the stock was stepped-up to its fair market value on the date of death of the surviving shareholders.

Tax Reform Act of 1976

The Tax Refom Act of 1976 provided that the basis of assets to an estate or heirs is, generally, the same as the decedent's basis in the asset, i.e., the basis is "carried over" from the decedent. As a result, the basis of stock to the heirs of a surviving shareholder is different under a cross-purchase agreement than from a stock redemption.

To convert a stock-redemption plan into a cross-purchase arrangement, shareholders must either incur the adverse tax consequences from the "transfer for value" rule or they must let the corporation's policies lapse and purchase new policies on the lives of their co-shareholders. The latter approach will almost always result in increased premium costs and will not be a viable alternative in cases where one or more of the shareholders have become uninsurable.

Issue

The issue is whether an exception to the "transfer for value" rule for the exclusion of life insurance proceeds should be provided to permit the changing of a stock-redemption plan into a cross-purchase plan.

Proposed Amendment

The proposed amendment would provide an exception to the "transfer-for-value" rule to permit the transfer of a life insurance contract by a corporation to a co-shareholder of the insured. This change would permit taxpayers to change stock-redemption plans into cross-purchase plans. Transfers for less than fair market value will, however, continue to be taxed as dividends to the extent provided in sec. 316 of the Code.

Revenue Effect

This provision will reduce budget receipts by less $1 million per year.

Departmental Position

The Treasury Department supports this amendment.

2. *Postponement of Generation-Skipping Tax*

Tax Reform Act of 1976

The Act imposes a tax in the case of generation-skipping transfers under a trust or similar arrangement upon the distribution of the trust assets to a generation-skipping heir (for example, a distribution to a great-grandchild of the grantor) or upon the termination of an interest of an intermediate generation in the trust (for example, the termination of an interest held by the transferor's grandchild). The tax will be substantially equivalent to the estate tax which would have been imposed if the property had been actually transferred outright to each successive generation.

In general, these provisions apply to generation-skipping transfers which occur after April 30, 1976. However, the provisions do not apply to any transfers under a trust which was irrevocable on April 30, 1976 (but only to the extent that the transfer is not made out of corpus added to the trust after April 30, 1976). In the case of a revocable trust or will in existence on April 30, 1976, the provisions will not apply if the grantor dies before January 1, 1982, and the trust instrument or will is not amended after April 30, 1976, in any way which increases generation-skipping. Where the grantor is incompetent, the grace period will be extended for a period of two years after the disability is removed.

Issue

The issue is whether the effective date of generation-skipping transfers to which the tax applies should be postponed.

Proposed Amendment

The proposed amendment would postpone the effective date of the tax on generation-skipping transfers until October 4, 1976, the date of enactment of the Tax Reform Act of 1976.

Revenue Effect

The revenue effect of this provision cannot be estimated because of lack of information about the particular trusts involved.

Departmental Position

The Treasury Department opposes this amendment.

3. *Estate Tax Exclusion for Certain Retirement Benefits*

Prior Law

Under prior law, the value of an annuity or other payment receivable by any beneficiary (other than the executor) under certain retirement programs was excludible from an individual's gross estate, except to the extent that the value is attributable to payments or contributions which were made by the decedent during his lifetime.

Tax Reform Act of 1976

The 1976 Act extended the estate tax exclusion to individual retirement accounts and to benefits payable on account of the death of a self-employed individual under an H.R. 10 plan.

The 1976 Act also provided that the estate tax exclusion would not apply in the case where benefits were received by a beneficiary as a lump-sum distribution. For this purpose, the estate tax exclusion does not apply if the distribution from the plan is "described" as a lump-sum distribution under the special 10-year averaging rules available for such distributions. This provision applies to estates of decedents dying after December 31, 1976.

Issues

The first issue is whether the elimination of the estate tax exclusion for lump-sum distributions should apply with respect to benefits attributable to employer contributions made before 1977.

The second issue is whether a lump-sum distribution should be eligible for the estate tax exclusion if the special 10-year averaging provision is not elected for income tax purposes.

Proposed Amendments

First, the estate tax exclusion for benefits under a qualified retirement plan would apply to the portion of a lump sum distribution attributable to employer contributions made before 1977. The amount eligible for the exclusion would be determined on the basis of the decedent's years of participation under the plan before 1977 compared to the total number of years of participation under the plan.

Second, the estate tax exclusion for benefits attributable to employer contributions would apply to a lump-sum distribution if special 10-year averaging is not elected for income tax purposes.

Revenue Effect

The first amendment will reduce budget receipts by $9 million in fiscal 1978, $8 million in fiscal 1979, $6 million in fiscal 1980, $5 million in fiscal 1981, $3 million in fiscal 1982, $2 million in fiscal 1983, and by a negligible amount thereafter.

The second amendment will reduce budget receipts by less than $1 million each fiscal year.

Departmental Position

The Treasury Department opposes both parts of this amendment. First, the availability of the estate tax exclusion is designed to give relief from the liquidity problems in an estate. Because there are no liquidity problems with a lump-sum distribution, the exclusion for these distributions was deleted. Treasury believes that there is no need for a grandfathering provision, because the 1976 Act applies only to estates of decedents dying after December 13, 1976. Those taxpayers who are concerned with the tax planning aspects of their distributions from pension plans are free to change the form of their distribution to maximize favorable tax treatment. Furthermore, the 1976 Act liberalized installment payments of estate tax and also provides new opportunities to postpone payment of estate tax. Second, the Treasury Department opposes the election of the estate tax exclusion. In the

1976 Act, the estate tax exclusion for lump-sum distributions was removed because these distributions do not pose liquidity problems for the payment of estate taxes. On the other hand, the favorable income tax treatment of lump-sum distributions (10-year forward avaraging is designed to ease the bunching effect on the income taxes of a one-time distribution. There is no reason to permit taxpayers to trade off one kind of tax break for another. These are separate issues, fully resolved in the 1976 Act.

4. Sections 6166 and 6166A—Extension of Time for Paying Estate Tax

Present Law

Code sections 6166 (added by the Tax Reform Act of 1976) and 6166A provide for an extended payment period for estate taxes where the decedent's estate consists largely of an interest in a closely held business. A closely held business includes certain corporations which have 15 or fewer shareholders (under section 6166) or 10 or fewer shareholders (under section 6166A). In determining the number of shareholders each individual is counted once without regard to any attribution rules (such as attribution between father and son).

Issue

The issue is whether attribution rules should be applied to permit stock held by the decedent's immediate family to be treated as held by a single shareholder in counting the number of shareholders for purposes of the estate tax extended payment provisions.

Proposed Amendment

The amendment would apply attribution rules for purposes of determining the number of shareholders in a corporation in applying sections 6166 and 6166A of the Code (relating to the extension of time for paying estate tax where estate consists of closelv held business). Under the rules, stock held by the decedent's immediate family (e.g., father, mother, spouse and descendents) would be treated as held by a single shareholder.

Revenue Effect

This provision will reduce budget receipts by less than $1 million per year.

Departmental Position

The Treasury Department opposes the amendment. Treasury believes that section 6161(a)(2) of the Code provides sufficient relief in these situations.

○